

# Analyzing the Jamaican Crisis

*Don Robotham*

**T**he first question to pose is: What is and is not the nature of the crisis? Jamaica is suffering from an all-around crisis that affects all sectors of public and private life and that involves the social, the political, and especially the economic system. Some people claim that this is a party political crisis; that is, if the political party in power were to change, the crisis would abate. However, although we certainly cannot absolve the existing political leaders of their responsibility for the extent and the prolongation of the crisis, they did not originate it.

Another approach is to argue that this crisis is constitutional. If Jamaica could only change from the Westminster parliamentary system to a U.S.-style presidential one, then it would be well on the way to resolving its problems. Those who advocate this solution display a charming but naïve faith in the power of constitutions—after all, mere pieces of paper—to bring about fundamental changes in a political situation. These notions are simply constitutional illusions.

Others argue that the root of our crisis is social. By this term they seem to be referring to the high crime rate, the growing inequities in the distribution of wealth, the condition of our inner cities, the poor performance in our education system, and our faltering health services. If we could only get our priorities straight and focus the reallocation of our resources in the social area, then we could begin to address our crisis effectively.

Again, this argument is a half-truth. Obviously, it would be highly desirable to effectively utilize more resources in such social areas. But where are these resources to be obtained? This is the resource illusion. There are many well-meaning persons in Jamaica who genuinely believe that “if only the government would provide more jobs,” then it would be on the way to addressing our problems. But how is the government to achieve this miracle in a market economy? Where will a government with a huge and growing foreign debt and a massive domestic debt get the funds to make such investments? The lack

of answers to these questions shows that people who say "government must provide more jobs" have not thought very carefully about what they are proposing.

I would say the adherents to this social and resource illusion exceed those who adhere to the religious and moral illusion—the values and attitudes argument. "What we need," according to that argument, "is a moral revolution in Jamaica." As I will argue, there is a very important moral dimension to our crisis, but the root of the situation is not moral.

What about the debt reduction argument? There are two problems with this argument that also make it illusory as a solution. First, Jamaica's problem is its domestic rather than its foreign debt. The second problem with debt relief is a far greater one: It offers only temporary short-run gains. It is not sustainable in the absence of larger economic changes, and it does not address the fundamental weakness of the economy.

### **A Production Crisis**

My argument is that to understand our crisis, we must look more deeply into the issues. Our fundamental problem is how to develop fresh resources for the economy. We have to grow the economy! Above all, given our dependence on imports for basic necessities (rice, flour, saltfish, oil) we have to expand our export earnings. Without such change, there is no hope. We have to achieve economic development or we will be dead in the water. But how are we to make these changes in a small, open economy subordinated to a globalized, deregulated market environment? How are we to divert funds from consumption into investment in an economy with an already low standard of living and harsh rural and urban poverty? We cannot deny the importance of equity.

It is undeniable that the fixed-exchange-rate-high-interest-rate mantra of the govern-

ment, as former leader of the National Democratic Movement, Bruce Golding, among others has repeatedly pointed out, necessarily meant a further upward redistribution of income. As the domestic debt spiraled past the foreign debt, Upper St. Andrew, the holder of this lucrative, high-interest-bearing government paper, became the nation's paymaster. Moreover, this way of dealing with our production crisis was necessarily a short-term solution. The domestic debt quickly fed on itself and became an insupportable burden on the very budget it was intended to relieve! Then came the banking crisis.

As the last six months of 2000 showed, this policy could not last. The government has had no choice but to commit to a steady reduction of interest rates, which means a steady reduction of the budget deficit and, of course, a steady devaluation of the Jamaican dollar and a reconstruction of the banking sector.

This relatively simple insight—that our basic problem is not only economic but is a matter of how we can get production and productivity to grow—is the fundamental point that is often missed in Jamaica today. Most politicians and most citizens speak as if they believe that there are funds available for "x" or "y" program. In our personal lives, our behavior is the same: If you were to travel around Kingston or the countryside, you would be shocked by the astonishing level of conspicuous consumption that seems to occur among all social classes—upper, middle, and lower. Despite the economic crisis, the current viewpoint seems to consider only how to spend money, not how to save or invest it.

But consumption is not our root problem. Our problem is deeper and more intractable—there is insufficient high-value-added productive activity in the formal sectors of the economy (especially the export sector) to generate the funds to be spent for

our social and personal needs. There is not enough money to finance health, education, transport, basic food imports, and oil at the level we need and to service our domestic and foreign debt. There is no legal money to satisfy the apparently insatiable demand for cars, vast houses, and name-brand clothing at the level of our personal needs. In an unproductive economy, there is no conceivable policy magic wand that can legitimately wish such funds into existence—not at the public or the private level. The economic cupboard is bare. This is the reality we hate to face.

If one accepts this very simple hypothesis—that the cupboard is bare—then a number of issues become clearer. There is no short-term solution to Jamaica's problems. Nor is there any sustainable personal solution for most except those who decide to embark on a criminal career. But there are medium- and long-term solutions. This is going to be a long haul, no matter who is in power.

### **No Shortage of Entrepreneurship**

In a market economy, it is private sector investment, not training, that is the key to economic expansion and job creation. Jamaica has no shortage of entrepreneurs itching to get into some kind of business activity. In fact, it may have too many! Drive down Hagley Park Road or around Eastwood Park or in and around Ocho Rios, and the dense proliferation of small businesses (dominated by motor vehicles and motor vehicle parts) cannot fail to strike you. You may also notice the development of many new and often ugly small "plazas" all over Kingston and in the country towns. Indeed, one of the hallmarks of Jamaica that makes our society and economy very different from those of Barbados and Trinidad is the rapid expansion of this black business class, which is highly stratified and strapped for cash and markets but is

pressing on regardless. Any idea that capitalist tendencies in Jamaica are a preserve of the old light-skinned landed and commercial elite may be buried once and for all.

This capitalist army, even though it may be investing mainly in "deportees," auto parts, and government paper at the moment, is perfectly capable with the right incentives of developing Jamaica into a modern economy with as high a standard of living as any in the world. In fact, they want and are itching to do just this. They are puzzled by the government's economic policy and the apparent lack of interest in them and in the obvious urgency of economic development. Black capitalists in particular, who actively campaigned for and supported Prime Minister P. J. Patterson, are at a loss. Why is the government ignoring them and their obviously irrepressible business initiative?

In simple terms, the key question for any investor, whether local or foreign, is what rate of return she will get on her investments. But if interest rates are at 22 percent, then why would any rational investors want to ensnare themselves with hard, fixed investment in the real economy? Consider also: If the exchange rate is uncompetitive, why invest for export from Jamaica? Because of the inflation of the Jamaican dollar, the U.S. dollar price fetched by the shirt made in Jamaica is one-third more than the price for the same shirt made in Mexico. Who will buy these uncompetitive Jamaican shirts? This high interest rate and uncompetitive exchange rate situation has been the problem in Jamaica for more or less the life of this government and is sufficient explanation for the lack of investment (indeed, disinvestment) in the real formal economy, especially for export.

The question then arises: Why has the government pursued this high-interest-rate and uncompetitive exchange rate policy? Obviously, the minister of finance, the governor of

the Bank of Jamaica, and many other government experts and senior civil servants are well aware that such a policy has an investment- and growth-killing effect. Why then has the policy been pursued?

### The Roots of Government Policies

The answer by now should be fairly clear: The high-interest-rate policy has been pursued in order to support a fixed exchange rate for the Jamaican dollar. Why has the government placed such emphasis on a fixed exchange rate, even when it was clearly uncompetitive and bound to damage the country's export earnings and therefore investment and job creation? Indeed, it is fair to say that a fixed exchange rate, even more than high interest rates, until recently was the alpha and omega of government economic policy under Minister of Finance Dr. Omar Davies.

The main reasons had to do with the 1970s and the early '90s and the PNP (Peoples National Party) government experiences with the devaluations of those times. In the 1970s, first under David Coore, then under the late Eric Bell and Hugh Small, the situation was disastrous, especially the notorious crawling-peg "depreciations" that served only to fuel daily and sometimes hourly price increases. Feroocious political responses via price inspectors proved impotent against the economic forces unleashed. More than any other single factor, these devaluations and the accompanying price increases undermined popular support for the PNP and helped to seal the JLP (Jamaica Labour Party) victory in 1980.

The experience with a floating exchange rate was no different under the second Michael Manley regime after 1989, when first P. J. Patterson and then Hugh Small were the finance ministers. It did not take much to convince a new PNP government that at all costs it must prevent a repeat of the earlier disas-

trous experience. It was imprinted on party officials' consciousness that a floating exchange rate meant weekly devaluations; weekly devaluations meant weekly increases in the price of basic imported foods such as rice, saltfish, and mackerel, not to mention such necessities as gasoline, kerosene, and electricity. Weekly cost-of-living increases were a sure road to weekly losses of political support.

The main economic task of the government therefore was to tame the devaluation beast and so to halt what had by then become the entrenched public expectation of continuous increases in the cost of basic goods. Targeting the exchange rate therefore became the thing to do as a means of drastically cutting inflation, stabilizing the cost of living, and ensuring political support for the government.

It must be admitted that the anti-inflationary goal of this policy objective has been achieved beyond the wildest dreams of the government—indeed, even beyond those of the general population. Many Jamaicans, young and old, seem to have no memory of the time, not too long ago, when they spent many days of the week shunting from one supermarket to the next, from one gas station to the next (remember those signs at the station entrances displaying the current gas prices?), hoping forlornly to beat what had by then become inevitable daily movements in the prices of basic necessities.

But people are not jumping for joy over the taming of inflation, and not rewarding the government politically, because of the price they have paid for this achievement: the devastation of the banking sector; the stagnation of the formal economy; the worsening of economic inequalities; the collapse of the labor market; and the aggravation of the general crisis in the economy, society, and political system. These outcomes were an inevitable consequence of using only one element of macroeconomic management—high interest

rates—to artificially stabilize another element—the exchange rate. The government lost sight of the fact that the goal was not simply to bring down inflation—it was to do so in a manner that created the most favorable incentives for investment and growth. The goal could not be simply to stabilize the exchange rate. It must be to stabilize the exchange rate on the basis of the real productive activity of the real export sector.

There was a policy alternative, but it was politically forbidding: Bring down inflation and stabilize the exchange rate at a lower level by sharply cutting the public sector deficit and instituting a tight interest-rate policy, but not at the astronomical heights to which the interest rate had been allowed to move. But the politics and social consequences of taking such a difficult policy course were daunting, to say the least.

In the end, in a deregulated market economy that is open to private merchandise, capital, and currency movements, the real exchange rate cannot be painlessly fixed by political fiat unless it has a sound basis in the real state of public finances. In other words, if there was a huge demand for our products and services overseas, and we therefore had a huge surplus in foreign trade and also in our balance-of-payments account, then of course we would accumulate large hard currency reserves from the funds paid to us from foreign sources. In other words, the now famous Net International Reserves (NIR)—the pride and joy of the minister of finance and the governor of the Bank of Jamaica—would be large because of the real earnings from foreign demand for our real productive export activities, or returns to us on real foreign investments.

### **“High Chest”**

The problem was that our exports were relatively small compared to our imports. To put

it simply, we were not producing anything foreigners considered worth much of their hard-earned hard currency. On the other hand, we lusted after what they produced: We wanted “Volvo and video,” but we had only bauxite, alumina, sugar, and tourism to sell. We therefore inevitably had both a chronic trade and a payment deficit. To put it in the vernacular, we had, and still have, “high chest”!

This deficit tended to grow as we consumed what foreigners produced and as foreigners realized that what we had to sell them in exchange did not amount to much. Left to the market alone, we would have had negative NIR to back the Jamaican dollar. Given this situation, the Jamaican dollar would inevitably be devalued to a position that reflected the real performance of our export production vis-à-vis our import consumption and the real resources that would or would not accrue to us from our net legitimate activities in international trade and finance.

But our cupboard was bare. There was and is no way under any sun that these productive activities could generate the foreign exchange reserves to support us in the style of national and personal consumption to which we have become accustomed. How then, in the absence of real competitive export performance from our real economy, to build up the NIR so as to stabilize the dollar, stabilize the cost of living, and bring down inflation? This was the economic and in a sense the social and political question faced by the Patterson government.

The answer was found in the simple policy expedient of relying solely on monetary policy—that is, raising Jamaican dollar interest rates to a level that would entice people to convert U.S. dollars into Jamaican dollars so as to capitalize on these lucrative high-interest-bearing Jamaican government securities. In a sense this was a devaluation, but one by

which the Central Bank benefited only the holders of large quantities of U.S. dollars in Upper St. Andrew and abroad. In effect, this wealthy group received a much higher rate of return on its U.S. dollars than did other Jamaicans (who had to make do with the official fixed exchange rate). This high-interest-rate policy would have the additional benefit of temporarily sopping up excess liquidity in the system, thereby helping to bring down inflation.

### The Bottom Drops Out

By such means were the coffers of our beloved NIR—the secret of our “stable” exchange rate—artificially filled in the absence of real earnings from a real improvement in our export performance. At what price was this victory won? First, a massive upward redistribution of income in Jamaican society was inherent in the policy. In effect, it meant buying the foreign exchange held by wealthy Jamaicans at an enormous premium, financed by high-interest-bearing government securities—in other words, by taxes paid by the rest of us. Second, we had to abandon all hope of investment in the real economy. Third, there was a massive increase in the domestic debt, which now far exceeds the foreign debt. Fourth, the policy precipitated a banking crisis that led to the almost complete collapse of the financial sector, which was driven from the field by the high-interest-rate regime.

Of course, no one could deny that greed, cupidity, corruption, malfeasance, ineptitude, naïveté, poor management, and a weak legal and regulatory regime all played a large part in bringing about and aggravating this extremely costly banking crisis for which our children will pay for generations to come. However, these were by no means the root cause of the crisis. The underlying cause was the high-interest-rate regime. People who

borrowed for investment purposes in the real economy at those high rates would find it extremely difficult to make an adequate rate of return on their investments to service these loans, at least not from legal activities in the formal economy. This situation inevitably meant the accumulation of a huge portfolio of bad debts by the banks. But “every day bucket go a well—one day, the bottom mus’ drop out!” And so it has.

There is now no choice but to reduce interest rates on Jamaican securities because the strain on the government budget is simply too great. This reduction means that the Jamaican dollar will have to be devalued in accordance with the performance (or rather, the lack thereof) of our export activity. The only real questions are: At what rate? At what social cost?

For one thing, it takes time for projects to be developed, for investments to come through, and for jobs to be created. There is a real possibility that just as we may be slowly (too slowly) getting our act together, the U.S. economy—our main export market—may be cooling off. In the meantime, the price increases that follow devaluation will take effect immediately. Furthermore, in order to control money supply, the government will also have to take action on the fiscal side: It will have to cut the government budget.

The problem in macroeconomic policy in Jamaica in the past, as economist Dr. Peter-John Gordon has often pointed out, is that one of the triad of macroeconomic stability was targeted but never all three: Government focused on the exchange rate but undermined these actions by ignoring the interest rate or the budget deficit. The upshot was that we got the worst of all possible worlds: devaluations, inflation, and no real improvement in our export competitiveness, coming full circle in a higher budget deficit. Above all, there was no economic growth.

But what the phrase "reducing the budget deficit" really means is the control of wage increases to a rate well below the rate of inflation and the possible laying off of thousands of workers from the public sector. We recently got a taste of this effect in the contretemps around the laying off of teachers by the Ministry of Education. More such actions are likely to come. Therefore, honest and full public discussion of how we plan to address the undoubtedly high social costs of this new policy period is urgently needed. It is necessary above all to patiently and repeatedly explain the economic thinking behind such a policy; the general public in Jamaica has no understanding of the need for consistency between monetary, fiscal, and exchange-rate policy.

Such a discussion must proceed with the understanding that, in broad outlines, a return to low interest rates, a competitive exchange rate, and a low budget deficit is the only way to attract sustained local and foreign investment and to unleash the considerable entrepreneurial talents of the Jamaican people for the sustained development of the real economy. Until now these entrepreneurial efforts have focused largely on trivial activities pandering to local consumption mania. With the change in the macroeconomic strategy, there is now a chance for this demi- or semiformal economy to return to the fold and to stimulate and shape the formal economy, which is where it belonged in the first place, and for economic growth to occur.

### **The Political Question: Ten Questions to Ask Any Political Party**

This analysis provides an approach to the political question. Which set of social forces is able to address the fundamental problems of the economy I have outlined? Who will say publicly what many know privately: that no

trade union settlement or contract or wage increase or scandalous salary increases and perks for managers can address our problems but in fact would serve only to aggravate them in the short term?

Which politician or group of politicians will tell the Jamaican people honestly that if the cupboard is really bare, then leadership can lead only by example: Leaders must, in their personal and managerial actions—perks, salaries, award of contracts, and so forth—be models of circumspection. The problem of consumerism in Jamaica is a broader and deeper one than moralizing about the extravagance of politicians and deploring the scandalously high salaries of some well-known public officials. After all, the politicians and public sector plutocrats are simply acting out with public funds the same extravagant lifestyle that many others are also indulging as part of the Jamaican status and social mobility game.

Of course, it is completely unacceptable that they are playing this game with public funds in an impoverished and stagnant economy. But a deeper problem is the social and cultural insecurity that prompts such behavior in the first place, in the society as a whole and among all social classes. Indeed, the popularity of the values inherent in "browning," of skin-lightening creams and name-brand clothes, of Lexus and Bimmer, in the inner city is as rampant as in the "outer city." The Jamaican people need to reject Jamaican and American hedonism, which is inimical to all forms of development, including capitalist development. We need to recover our tradition of Black Protestantism, which has been the basis of much of the development that we have achieved. Saving, fear of debt, cautious expenditure, and modesty in all things have been a profound part of our rural culture and the source of our success as emigrants.

The political question has two dimensions: Which coalition of classes has a vital interest in resolving the crisis and the capacity to address it? More concretely, which political group is actually developing a program that actually identifies the true nature of the crisis and outlines a realistic platform for addressing it?

Given the depth of the crisis, the answer to the first question must be that we need an unprecedented level of all-class unity in Jamaica. The economic and social emergency is of such great proportions that it will not be solved unless the wealthiest capitalists and the smallest farmers can agree on a common program for action. Old or new political allegiances are of little use to us at this juncture.

As for the second question—a concrete political platform—this latter objective will take years of public discussion to achieve. If it is to be developed merely as a public relations election exercise, that would be a sure sign that such a party is unfit to rule. I will therefore set out some questions, the answers to which would provide the elements of such a platform prior to any election:

1. Exactly how do we propose to bring down interest rates so as to stimulate investment in the real economy? Over what time frame is this goal to be achieved?
2. Exactly how do we propose to reduce the budget deficit, to what figure, and over what period of time?
3. Exactly how do we propose to ensure that we have a competitive exchange rate?
4. Exactly how do we propose to ensure that these three elements of macro-economic stability proceed in harmony and not at odds with each other, as in the recent past?
5. Exactly how do we propose to cushion the high social costs of this adjustment, especially for rural and inner-city residents?
6. Exactly how and over what period of time do we propose to transform the police force, eliminate corruption, and break the political connections with garrison communities in order to reduce the crime rate? (I say “transform” rather than “reform” because I do not rule out the possibility of dissolution and rebuilding from scratch.)
7. Exactly how and over what period of time do we propose to improve the performance of our education system, especially the fit with the labor market and the reduction of the dropout rate of young males?
8. Exactly how do we propose to reduce police brutality; protect and improve the human rights of all, especially poorer citizens; and ensure speedy and fair justice?
9. Exactly how do we propose to address the growing socioeconomic inequality in Jamaica, especially in the rural areas and inner cities, and to bring about a more equitable and cohesive society?
10. Exactly how do we propose to reduce conspicuous consumption in Jamaica, and what personal examples do we intend to set at all levels of the society?

I believe that the issues pinpointed in this list are the decisive ones for economic growth and job creation and for pulling ourselves out of our crisis. At least these questions will spare us the charade of the usual grandiose and comical promises emanating from those in power, for instance, the promise to develop a huge “world-class” chemical complex or to attract “massive foreign investment” to Ja-



maica, miraculously solving all our employment and foreign exchange problems in one fell swoop. Such projects are, of course, complete pie in the sky designed to impress a credulous electorate.

Likewise, let us be spared the sankeys<sup>2</sup> about “values and attitudes,” “deepening democracy,” or enhancing our “national sovereignty.” Let us tone down the largely inane chatter about “constitutional reform” and declare a moratorium on the clever manipulations of cultural politics—cynical attempts to cash in politically on people’s feelings—by not naming for the time being any popular figures from our past as new national heroes. Nor should those unable to finance their relatively

modest private business operations, or to pay their General Consumption Tax (the Jamaican value-added tax) or other taxes on time, be allowed to indulge in their usual vainglorious pontifications on “what Jamaica needs now.”

### Notes

1. The idea of being light-skinned and “European” as status-enhancing.

2. A “sankey” is Jamaican sarcastic slang for what the English call cant, or insincere phraseology. It comes from Ira David Sankey (1840–1908), who was a U.S. popularizer of missionary hymns, especially in the nineteenth-century religious revivals that led to the spread of Pentecostalism. These hymns exhorted the poor to temperance and other forms of pious behavior, which missionaries thought good for their soul.